

Message Text

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INFO OCT-01 ISO-00 AID-20 CEA-02 CIAE-00 COME-00 EB-11

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O 071830Z NOV 73

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TO SECSTATE WASHDC IMMEDIATE 1038

LIMITED OFFICIAL USE SECTION 1 OF 3 OECD PARIS 28776

E.O. 11652: N/A

TAGS: ECON, EFIN, OECD

SUBJECT: SHORT-TERM FORECASTERS MEETING, NOV. 5-6

DEPT PASS CEA, FRB(BRIMMER), TREAS, COMMERCE

REF: DES/NI/F(73)3

1. SUMMARY: FORECASTERS REJECTED SECRETARIAT THESIS THAT DANGER FOR ECONOMIC POLICY MAKERS LIES ON SIDE OVERKILL, AND THEY DID NOT FORESEE LIKELIHOOD CUMULATIVE DDOWN TURN. COUNTRIES EXPECTED CONTINUE EMPHASIZE CONTAINING INFLATION. EXPANSION FOREIGN TRADE THIS YEAR WOULD BE A RECORD AND SLOWER BUT STILL HIGH RATE FORECAST FOR NEXT YEAR. DISCUSSION OIL AND TRADE WITH LDC'S LIMITED BY UNCERTAINTIES AND BY LARGE MARGINS ERROR IN MAKING FORECASTS. END SUMMARY.

2. OUTPUT. SECRETARIAT FORECASTS FOR GROWTH OF GNP IN 1973 AND 1974 VERY CLOSE TO INDIVIDUAL COUNTRY EXPECTATIONS. GROWTH RATE FOR OECD AREA SEEN DECLINING
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FROM 6.8 PERCENT IN 1973 TO 4.25 PERCENT IN 1974, WHILE

ON BASIS COUNTRY FIGURES IT WOULD BE 6.5 PERCENT AND 4 PERCENT. FOR 1973, ALL COUNTRIES, AND ESPECIALLY ITALY, SAW GROWTH RATES LOWER OR EQUAL TO SECRETARIAT FORECAST. FOR 1974, CANADA, UK AND US ESTIMATED HIGHER GROWTH THAN SECRETARIAT, ITALY, FRANCE AND JAPAN FORECAST LOWER GROWTH, WHILE GERMANY AGREED WITH SECRETARIAT PREDICTIONS.

3. SECRETARIAT NOTED THAT ITS FORECASTS FOR 1974 HAD BEEN REVISED CONSISTENTLY DOWNWARDS SINCE LAST SPRING DUE TO EXPECTATION THAT RAPIDLY RISING PRICES WOULD RESTRAIN GROWTH OF REAL DEMAND. IT THOUGHT THERE WAS DANGER NOW OF POSSIBLE OVERKILL IF CURRENT PROGRAMS OF RESTRAINT IN MANY OECD COUNTRIES MAINTAINED TOO LONG. HOWEVER, RECESSION UNLIKELY IN VIEW BUSINESS INVESTMENT IN FIXED ASSETS AND STOCKS. GENERAL RESPONSE OF COUNTRIES WAS THAT OVERKILL NOT LIKELY IN FACE CONTINUED MODERATE GROWTH IN 1974 AND HIGH LEVELS OUTPUT. POSSIBILITY CUMULATIVE DOWNTURN CLEARLY NOT ENVISAGED BY MAJOR OECD COUNTRIES, AND CONTINUED EMPHASIS ON CONTAINING INFLATION WILL BE NECESSARY WHILE CAPACITY REMAINS TIGHT.

4. US DEL (FOSS) SUMMARIZED EXPECTATIONS FOR THIRD AND FOURTH QUARTER 1973, BUT DECLINED PREDICT 1974 DEVELOPMENTS IN SPECIFIC TERMS. HE NOTED SIGNS OF WEAKENING DEMAND BUT CONSIDERED SECRETARIAT COMMENTS THIS AREA WERE OVERSTATED. ALTHOUGH HOUSING STARTS WERE DOWN, DEMAND FOR CAPITAL GOODS AND EXPORTS REMAINED HIGH, AND OUTPUT LEVELS WOULD PROBABLY BE HIGHER THAN SECRETARIAT FORECAST. IN QUESTION PERIOD AFTERWARDS, COUNTRIES EXPRESSED INTEREST IN WAGE PROSPECTS, CAPACITY GROWN, EFFICIENCY OF PHASE IV, STATE AND LOCAL EXPENDITURE LEVELS, EXPORT PRICE TRENDS, AND POSSIBLE SIGNS WEAKENING DEMAND. US DEL NOTED THAT WAGE INCREASES WOULD PROBABLY BE GREATER IN 1974 THAN IN 1973, BUT THERE WERE NOT AS MANY LARGE CONTRACTS DUE FOR NEGOTIATION. CAPACITY GROWTH HAD BEEN SLOW OVER PREVIOUS FIVE YEARS AND WOULD INCREASE ONLY GRADUALLY. PHASE IV SUCCEEDED IN SLOWING DOWN RAPID PRICE RISES IN INDUSTRIAL SECTOR, BUT SOME LIMITED OFFICIAL USE

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PROBLEM OF PRODUCERS SHIFTING FROM CONTROLLED DOMESTIC TO UNCONTROLLED FOREIGN MARKETS. RE SECRETARIAT SUGGESTION THAT FALLING INTEREST RATES AND STAGNANT MONEY SUPPLY INDICATED POSSIBLE WEAKENING DEMAND, US DEL DISAGREED AND CITED CONTINUING RISE IN DEMAND FOR BUSINESS LOANS AND SHIFT INTO COMMERCIAL PAPER. FINALLY, HE CAST DOUBT ON CAPACITY UTILIZATION FIGURES PUT FORWARD BY SECRETARIAT AND SUGGESTED THESE FIGURES APPEARED TO

UNDERESTIMATE TIGHT SITUATION IN US, GERMANY, JAPAN, ,
UK AND ITALY.

5. JAPANESE DEL GAVE DIFFERENT PICTURE FROM COLLEAGUE
AT WP4 WHO HAD INDICATED GRAVE CONCERN RE DANGER OVER-
KILL. PRESENT FORECAST WAS THAT VERKILL NOT PROBLEM
AT PRESENT BUT RATHER NEED FOR PRICE STABILIZATION AT
TIME OF CAPACITY SHORTAGE. JAPAN INTENDS MAINTAIN
RESTRICTIVE MONETARY AND FISCAL POLICIES INTO NEXT YEAR.

6. GERMAN DEL AGREED GENERALLY WITH SECRETARIAT
ASSUMPTIONS AND FORECASTS, BUT QUESTIONED PREDICTION
THAT INVESTMENT TAX WOULD BE REMOVED BY MID-1974.
GERMANS CONSIDERED IT VERY IMPORTANT NOT TO SIGNAL MAJOR
CHANGES IN RESTRICTIVE POLICIES FOR FEAR EXCESSIVE WAGE
CLAIMS. THEY ALSO NOTED IN RESPONSE SECRETARIAT QUETION
THAT PUBLIC EXPENDITURE LIKELY INCREASE STRONGLY IN
1974 DESPITE EFFORTS RESTRAIN LOCAL GOVERNMENT SPENDING.

7. OTHER COUNTRIES. ITALY SAW CONSIDERABLY LOWER
INCREASE IN GNP THAN SECRETARIAT FOR 1974 DUE TO PESSI-
MISTIC EXPECTATIONS REGARDING EXPORT DEMAND AND
LIMITATIONS ON PRODUCTION CAPACITY. UK IN GENERAL
AGREEMENT WITH SECRETARIAT, ALTHOUGH SEEING HIGHER
CONSUMPTION LEVELS AND SLIGHTLY HIGHER OUTPUT THAN
SECRETARIAT FORECASTS FOR 1974. CANADA, FRANCE ALSO
INGENERAL AGREEMENT.

8. COUNTRY FORECASTS VERSUS SECRETARIAT FORECASTS
FOR REAL GROWTH OF GNP FOLLOWS:

	1973		1974	
	SECT.	COUNTRY	SECT.	COUNTRY
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CANADA	7.3	7.2	5-1/4	5-1/2
FRANCE	6.3	6.1	5-3/4	5
GERMANY	6.2	6.0	3-1/2	3-1/2
ITALY	5.6	5.0	7-1/2	6
JAPAN	11.7	11.7	8-1/2	7-3/4
UK	6.8	6.5	3-1/2	4
US	6.2	6.0	2-1/2	(HIGHER)
TOTAL OECD	6.8	6.5	4-1/4	4

9. PRICES: SECRETARIAT FORECAST 6.9 PERCENT PRICE
INCREASE FOR TOTAL OECD IN 1973 WAS CONSISTENT WITH
COUNTRY FORECASTS, ALTHOUGH JAPAN, ITALY, GERMAN AND
US THOUGHT THEIR PRICE FORECASTS WERE SOMEWHAT HIGH,
AND UK THOUGHT ITS FORECAST MUCH TOO LOW. FOR 1974,
SECRETARIAT FORECASTS WERE GENERALLY HIGHER THAN

INDIVIDUAL COUNTRY FORECASTS, SECRETARIAT VIEW OF
1974 WAS THAT TRANSACTIONS PRICES WOULD CONTINUE RISE
DURING FIRST HALF YEAR FOLLOWING SPOT PRICE RISES OF
1973, AND THEN LEVEL OFF. MOST COUNTRIES CONSIDERED
CRITICAL UNKNOWN FACTORS TO BE THE STILL UNDETERMINED
IMPACT OF OIL PRICE RISES AND SUPPLY CUTBACKS, AND
WAGE RESPONSES TO 1973 PRICE RISES.

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10. US EXPECTED PRICES WOULD RISE BY SLIGHTLY LESS
THAN SECRETARIAT FORECAST OF 5.3 PERCENT IN 1973 AND
6.0 PERCENT IN 1974. US DEL NOTED CONTINUED DOWN-
WARD TREND IN FARM PRICES, AND EXPRESSED DOUBT RE SECRE-
TARIAT ASSUMPTION THAT TRANSACTIONS PRICES WOULD FAITH-
FULLY FOLLOW SPOT MOVEMENTS. HE ALSO CONSIDERED WAGE
FORECASTS OF SECRETARIAT TO BE EXCESSIVE, SINCE RATE
OF INCREASE OF WAGES WAS DECLINING.

11. OTHER COUNTRIES: JAPAN CONSIDERED PRICE STABILIZA-
TION TO BE ITS MOST URGENT PRIORITY IN VIEW CPI IN-
CREASE OF ALMOST 15 PERCENT OVER PAST YEAR. GERMANY
SEEMED CONFIDENT THAT WAGE PRESSURES COULD BE CONTAINED
IN SPITE OF EXPECTED DEMANDS FOR 12-15 PERCENT INCREASES

NEXT YEAR. EXTENT OF WAGE INCREASES WOULD DEPEND ON DEVELOPMENTS ON PRICE FRONT AND ON CONTINUED DEMONSTRATION OF GOVERNMENT COMMITMENT TO PRICE RESTRAINT. FRANCE WAS UNABLE EXPLAIN HOW IT HOPED BRING PRESENT 10 PERCENT NEXT YEAR. UK AS CONCERNED THAT OIL DEVELOPMENTS MIGHT PUSH PRICE RISES ABOVE 6 PERCENT THRESHOLD LINE AT WHICH WAGE INCREASES BECOME AUTOMATIC, ESPECIALLY LIMITED OFFICIAL USE

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IF OIL PRICE RISES ARE ONLY EMPORARY. ITALY REPORTED SUCCESS OF PRICE FREEZE IN REDUCING CPI GROWTH BY HALF SINCE IMPOSITION IN JULY. CANADA SURPRISINGLY INDICATED LITTLE CONCERN RE DANGER OF WAGE EXPLOSION, IN VIEW OF POSITION TAKEN AT WP4 WHERE SITUATION DESCRIBED AS POTENTIAL WAGE VOLCANO.

12. DIFFERENCES BETWEEN SECRETARIAT AND COUNTRY FORECASTS OF GNP DEFLATOR FOLLOWS:

	QOUE		QOUR	
	SECT.	COUNTRY	SECT.	COUNTRY
CANADA	6.3	6.3	6-3/4	6-1/4
FRANCE	6.8	7.2	7-1/2	7-1/4
GERMANY	6.4	6.0	6-3/4	6-1/2
ITALY	11.1	10.8	9-1/2	8
JAPAN	10.4	9.4	9	7-3/4
UK	5.7	8.0	5-1/2	-
US	5.3	5.1	6	-
TOTAL OECD	6.9	6.9	7	6-3/4

13. TRADE AND PAYMENTS: MEMBERS CONFIRMED SECRETARIAT'S FORECAST OF RECORD OECD TRADE IN 1973 - A 13/14 PERCENT VOLUME INCREASE IN IMPORTS

AND CLOSE TO 15 PERCENT IN EXPORTS, COMPARED WITH 1972. FOR 1974, THE SECRETARIAT AND PARTICIPANTS PRETTY MUCH AGREED THAT IMPORTS MIGHT RISE SOMEWHAT OVER 10 PERCENT AND EXPORTS BY ABOUT 11 PERCENT.

14. U.S. (LEADERER) SAID ITS TRADE ACCOUNT HAD PERFORMED BETTER THAN ANTICIPATED IN THIRD QUARTER AND IMPROVEMENT OVER 1972 WAS ON ORDER OF \$10 BILLION AT ANNUAL RATE. FOR SECOND HALF 1973, BOTH TRADE AND CURRENT ACCOUNTS WOULD BE IN SUBSTANTIAL SURPLUS RATHER THAN SECRETARIAT'S FORECAST OF \$100 MILLION DEFICITS FOR EACH. FOR YEAR 1973, U.S. EXPECTED TRADE SURPLUS BE ON ORDER OF \$900 MILLION AND CURRENT ACCOUNT ABOUT \$1.3 BILLION. BECAUSE LARGE MARGINS ERROR LIKELY IN 1974 FORECASTS, U.S. GAVE NO FIGURES, BUT THOUGHT SECRETARIAT'S NOT TAKING INTO ACCOUNT OIL PRICE INCREASE.

15. FRENCH EXPECTED SLOWDOWN IN GROWTH EXPORT MARKETS FROM 8.1 PERCENT IN 1973 TO ABOUT 3 PERCENT IN 1974 IN RESPONSE TO SLOWER GROWTH RATES IN PRINCIPAL TRADING PARTNERS AND RELATIVELY HIGHER

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PRICES FOR FRENCH EXPORTS. FRENCH DEL EXPRESSED APPREHENSION ABOUT "OVER-COMPETITIVENESS" U.S. ECONOMY BECAUSE OF "OVER-DEVALUATION" DOLLAR. UNDER QUESTIONING FROM U.S., HE WAS UNABLE DEFINE OR EXPLAIN SUBSTANCE OF THESE TERMS. GERMAN QUESTIONS BROUGHT OUT THAT LOWER MARKET SHARE OF 3 PERCENT IN 1974 WAS ONLY WORKING ASSUMPTION.

16. GERMAN DEL SAID A DECLINE IN REAL TERMS OF EXTERNAL ACCOUNT WAS PROBABLE IN 1974. HE THOUGHT 1973 EXPORT MARKET GAINS OF 3 PERCENTAGE POINTS MORE LIKELY THAN SECRETARIAT'S 5 POINTS. GERMAN DEL COMMENTED THAT EXPORTERS HAD COMPETITIVE ADVANTAGE BECAUSE THEY WERE ABLE OFFER SHORTER DELIVERY DATES AND INDUSTRY GAVE PREFERENCE TO EXPORT RATHER THAN DOMESTIC MARKET. EXPORTS TO U.S. AND CANADA HAD DEVELOPED DISPROPORTIONATELY DESPITE EXCHANGE RATE ADJUSTMENTS, AND SALES TO U.K. AND IRELAND AS NEW MEMBERS COMMON MARKET HAD RISEN SHARPLY. EXPORTS TO JAPAN WERE UP 38 PERCENT AND TO EASTERN EUROPE 40/45 PERCENT. DEL SAID 1973 CURRENT BALANCE LIKELY BE 2.5 BILLION SDR'S RATHER THAN SECRETARIAT'S 2.9 BILLION, AND TRADE BALANCE 11.9 BILLION SDR'S COMPARED WITH SECRETARIAT'S 11.3 BILLION.

17. JAPANESE SAID THEIR TRADE AND PAYMENTS FORECASTS AGREED WITH SECRETARIAT'S IF OIL PRICE INCREASES WERE TAKEN OUT. THESE PRICE RISES WOULD ADD ABOUT 250 MILLION SDR'S TO IMPORT BILL IN 1973 AND ABOUT 1.5 BILLION IN 1974. FOR 1973/74 THEY ESTIMATED THAT BOTH EXPORTS AND IMPORTS WOULD BE SOMEWHAT HIGHER IN TERMS OF PRICE AND LOWER IN VOLUME THAN SECRETARIAT'S FORECASTS. THEY WERE ASSUMING EXCHANGE RATE OF 265 YEN/DOLLAR. HOWEVER, IF PRICES OF COMMODITIES, INCLUDING OIL, CONTINUE TO RISE, THERE WOULD BE LARGER CURRENT BALANCE

DEFICIT IN 1974. THEY EXPECTED CONTINUATION SIZEABLE CAPITAL OUTFLOWS. UNDER THESE CIRCUMSTANCES, JAPAN COULD NOT KEEP A "SUPER-CLEAN FLOAT" AT 265 YEN/DOLLAR BUT RATE COULD GO UP TO 300 NEXT YEAR. THEY FORECAST FOR 1973 A CURRENT BALANCE OF 700 MILLION SDR'S AND A TRADE BALANCE OF 3.5 BILLION. IN RESPONSE U.S. QUESTION, JAPANESE SAID THEIR FORECASTS ASSUMED NO ADDITIONAL EXPORT OR IMPORT RESTRAINTS.

18. ITALIANS THOUGHT THEIR EXPORT PERFORMANCE WOULD NOT BE AS GOOD AS SECRETARIAT'S FORECAST FOR 1973 BECAUSE OF HIGH DOMESTIC DEMAND, CAPACITY LIMITATIONS, ESPECIALLY IN TEXTILES AND CHEMICALS, AND "BOTTLENECKS" IN AUTO INDUSTRY. THEY EXPECTED CURRENT BALANCE DEFICIT OF 1.4 BILLION A TRADE DEFICIT OF 2.8 BILLION. FOR 1974,
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THE RESPECTIVE DEFICIT FIGURES ARE \$1.1 BILLION AND 3.1 BIL, A SHARP

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DIFFERENCE WITH SECRETARIAT'S FORECAST OF \$1 BILLION SURPLUS ON CURRENT BALANCE. THIS SEEMED DUE MAINLY TO DIFFERENT INTERPRETATION OF EXPORT PERFORMANCE AND SECRETARIAT'S EXPECTATION LARGER TOURISM RECEIPTS AND MIGRANT WORKERS' REMITTANCES.

19. UNITED KINGDOM DEL SAID THAT THEIR TRADE BALANCE FORECAST ON PRE-OIL BASIS DIFFERED ONLY LITTLE FROM SECRETARIAT'S BUT THEY HAD LOWER EXPORT AND IMPORT FIGURES. THEY ESTIMATED OIL PRICE HIKE OF 40 PERCENT WOULD CUT OIL IMPORTS BY ABOUT 8 PERCENT, BUT THEY WERE UNCERTAIN ABOUT AFFECTS FURTHER SUPPLY CUTBACKS ON IMPORT DEMAND IN VIEW INELASTIC INDUSTRIAL NEEDS. THEY FORECAST 1973 DEFICITS IN CURRENT BALANCE AT \$2.5 BILLION AND TRADE BALANCE AT \$4.5 BILLION. IN 1974, THEY EXPECTED FOREIGN DEMAND TO BE CONSIDERABLY LESS THAN IN 1973. U.K. DEL SAID THEIR FORECAST WAS ON BASIS UNCHANGED POLICIES, AND DESPITE ANTICIPATED RISE IN DOMESTIC CONSUMPTION, THERE WOULD STILL BE SUFFICIENT CAPACITY TO EXPAND EXPORTS NEXT YEAR. HE ALSO TOLD U.S. QUESTIONER THAT RELAXATION OF PRICE AND INCOME CONTROLS IN STAGE 3 WAS NOT TOO SIGNIFICANT AND THAT ECONOMY WOULD REMAIN EXPORT ORIENTED.

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20. CANADIANS AGREED WITH SECRETARIAT'S 1973 CURRENT BALANCE FORECAST OF ABOUT \$550 MILLION, ALTHOUGH THEY THOUGHT \$600 WOULD BE CLOSER TO OUTCOME. SECRETARIAT WAS, HOWEVER, FORECASTING \$100 MILLION LARGER TRADE SURPLUS THAN CANADIANS. DEL SAID EXPORT AND IMPORT VOLUME WAS LOWER THAN SECRETARIAT'S FOR 1973 AND SUBSTANTIALLY LESS IN 1974, BUT THEIR PRICE EXPECTATION WAS IN LINE WITH SECRETARIAT'S THEY NOTED OECD SEEMED PUT MORE WEIGHT THAN THEY DID ON INCREASED IMPORTS MACHINERY AND EQUIPMENT. CANADIANS EXPECTED CURRENT BALANCE IN 1973 BE IN DEFICIT BY ABOUT CAN. \$1 BIL AND ABOUT 430 MILLION AND 2.2 BILLION. FOREGOING ASSUMES NO CHANGE IN OIL TRADING POLICY AND APPARENTLY TAKES NO ACCOUNT OF OIL PRICE RISE. SECRETARIAT AGREED REVISE 1973 EXPORT AND IMPORT FIGURES DOWNWARD, BUT THEY FOUND IT HARD TO SQUARE CANADIAN 1974 EXPECTATION OF 5-1/2 PERCENT IMPORT VOL INCREASE WITH 5-1/2 PERCENT REAL GROWTH GNP.

21. TRADE WITH LDC'S: GENERAL CONCLUSION BRIEF DISCUSSION THIS TOPIC WAS THAT MARGIN OF ERROR ON ESTIMATES WAS SO LARGE THAT THERE WAS NO POINT IN DEBATING DIFFERENCES BETWEEN SECRETARIAT'S FIGURES AND THOSE OF IMF. LATTER SUGGESTED 20 PERCENT INCREASE OECD EXPORTS TO NON-OECD LDC'S COMPARED WITH SECRETARIAT'S 17 PERCENT. IMF DEL SAID PEAK OF COMMODITY BOOM MIGHT HAVE BEEN PASSED LATE LAST SUMMER OR EARLY AUTUM AND ONE COULD EXPECT, RAPID INCREASE IN SUPPLY AGRICULTURAL COMMODITIES, AND LIKELY ABSENCE EXCHANGE RATE SPECULATION, SHOULD LEAD TO SOME SOFTENING IN PRICES, WITH ACCELERATED DECLINES IN SECOND HALDF 1974.

22. OIL: THERE WAS LIMITED DISCUSSION OF EFFECTS OIL PRICE HIKE AND SUPPLY CUTBACKS ON OECD MEMBERS' IMPORTS AND ECONOMIES. SECRETARIAT GOT VIRTUALLY NO RESPONSE TO PROVOCATIVE QUESTION WHETHER CUTBACKS COULD BE MET BY RESTRICTIONS ON AUTO-MOBILE USE AND HOME HEATING OR WHETHER INDUSTRIAL OUTPUT WOULD BE SERIOUSLY AFFECTED. IT ALSO NOTED THAT INCREASED INCOMES OPEC COUNTRIES MIGHT NOT LEAD TO INCREASED OECD EXPORTS BECAUSE OF LIMITED ABSORPTIVE CAPACITY OPEC COUNTRIES. ALSO SUGGESTED POSSIBLE ADVERSE IMPACT OF OIL PRICE RISE IN PURCHASING POWER OF NON-OIL DEVELOPING COUNTRIES.. HOWEVER, DELEGATES UNWILLING TACKLE THESE QUESTIONS AT TIME WHEN COUNTRIES WERE STILL ASSESSING SITUATION AND HADN'T COME TO FULL
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CONCLUSION YET. U.S. DEL (LEDERER) EXPLAINED COMPLICATIONS

OF DETERMINING ACCURATELY LANDED COST OF OIL. U.K. AND
NETHERLANDS SAID THERE WAS SOME OPPORTUNITY TO FIND
SUBSTITUTES FOR OIL. UK NOTED CUTBACK OIL SUPPLIE OF ORDER
15 PERCENT WOULD NOT HAVE TOO SERIOUS IMPACT ON ECONOMY BEC-
AUSE THEY HAD GREAT POSSIBILITY STANDBY COAL FIRED POWER
STATIONS INTO LINE TO REPLACE THOSE OIL FIRED.
BROWN

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